84-1868

No. 84-____

Office Supreme Court, U.S.
FILED
MAY 29 1985
ALEXANDER L. STEVAS,
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

PENNZOIL COMPANY,
Petitioner,

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

Of Counsel:
JOHN B. CHAPMAN
PENNZOIL COMPANY
Post Office Box 2967
Houston, Texas 77001

C. E. GOODWIN
GOODWIN & GOODWIN
500 Church Street
Ripley, West Virginia 25271

BRUCE F. KIELY
Counsel of Record
KIRK K. VAN TINE
BAKER & BOTTS
1701 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 457-5500
Attorneys for Petitioner Pennzoil Company

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTION PRESENTED FOR REVIEW

1. Whether the Supreme Court of Appeals erred by upholding a decision of the Public Service Commission of West Virginia that purports to set a wellhead price for a "first sale" of natural gas in interstate commerce in violation of the intent of Congress, in conflict with the prior decisions of this Court and in disregard of the previous decision of the Supreme Court of the United States in a related case?

PARTIES BELOW

The Petitioner in this case who participated in the case below is:

Pennzoil Company *

The other parties in the case below were:

Public Service Commission of West Virginia

---

* The following companies are the non-wholly owned subsidiaries of Pennzoil Company: National Transit Company; Pennesco, Inc.; and the Eureka Pipe Line Company.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED FOR REVIEW	i
PARTIES BELOW	ii
OPINIONS AND ORDERS BELOW	1
JURISDICTION	2
STATUTES INVOLVED	2
STATEMENT OF THE CASE	2
A. Introduction	2
B. Facts	5
C. The Provisions Of The NGPA At Issue	9
D. The Decision of This Court in *Mid-Louisiana*	10
E. The Effect of the FERC Final Rule Implementing *Mid-Louisiana*	11
REASONS FOR GRANTING THE WRIT	12
A. Pennzoil's Production in West Virginia is Not Subject to Section 602 of the NGPA	12
B. The West Virginia Legislature Has Chosen Not To Exercise Its Authority Under Section 602	17
C. Section 602 Precludes Establishment Of Rates On A Case-By-Case Basis	18
D. Potential Consequences Of The Commission's Assertion of Authority	20
CONCLUSION	22
APPENDICES	

TABLE OF AUTHORITIES

CASES — Page

California v. Lo-Vaca Gathering Co., 379 U.S. 366 (1965) 13
Deep South Oil Co. v. FPC, 247 F.2d 882 (5th Cir. 1957) 13
Energy Reserves Group v. Kansas Power & Light Co., 459 U.S. 400, 103 S. Ct. 697 (1983) 9, 22
Exxon Corp. v. Eagerton, 103 S. Ct. 2296 (1983) 9, 14, 19
FPC v. Amerada Petroleum Corp., 379 U.S. 687 (1965) 13
Hecht Co. v. Southern Union Co., 474 F. Supp. 1022 (D.N.M. 1979) 20
Louisiana Public Service Comm'n v. FPC, 359 F.2d 525 (5th Cir.), *cert. denied*, 385 U.S. 833 (1966) 13
Maryland v. Louisiana, 451 U.S. 725, 101 S. Ct. 2114 (1981) 9
Mid-Louisiana Gas Co. v. FERC, 664 F.2d 530 (1981) *reh'g denied*, 669 F.2d 729 (5th Cir. 1982) 12, 16
Oklahoma v. FERC, 494 F. Supp. 636 (W.D. Okla. 1980), *aff'd* 661 F.2d 832 (10th Cir. 1981), *cert. denied sub nom. Texas v. FERC*, 457 U.S. 1105 (1982) 9
Pennzoil Co. v. Public Service Commission of West Virginia, —— U.S. ——, 103 S. Ct. 3564 (1983) 2
Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 22
Phillips Petroleum Co. v. Wisconsin, 347 U.S. 672 (1954) 22
Public Service Comm'n of New York v. Mid-Louisiana Gas Co., —— U.S. ——, 103 S. Ct. 3024 (1983) ..... *passim*
Public Service Comm'n of Kentucky v. FERC, 610 F.2d 439 (6th Cir. 1979) 14

STATUTES

Natural Gas Act of 1938, 15 U.S.C. §§ 717
Section 1(b), 15 U.S.C. § 717(b) 7
Section 7(b), 15 U.S.C. § 717f(b) 7

TABLE OF AUTHORITIES—Continued

Page

Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-3421 ..... *passim*

Section 2(21), 15 U.S.C. § 3301(21) 10
Section 2(34), 15 U.S.C. § 3301(34) 17
Section 503, 15 U.S.C. § 3413 17
Section 602, 15 U.S.C. § 3432 ..... *passim*

28 U.S.C. § 1257(3) 2
Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. §§ 55-1401 to 1415 (Supp. 1980) 20
Oklahoma Natural Gas Price Protection Act, 52 Okla. Stat. Ann. §§ 260.1 to 260.13 (Supp. 1980) 20
New Mexico Natural Gas Pricing Act, N.M. Stat. Ann. §§ 62-7-1 to 62-7-10 20
West Virginia Code

§ 24-1-1(a)(4) 8
§ 24-2-13 18

ADMINISTRATIVE AUTHORITIES AND REGULATIONS

FERC Order No. 391, 28 Fed. En. Reg. Comm. (CCH) ¶ 61,263 (Aug. 22, 1984); 49 Fed. Reg. 33,849 11

OTHER SOURCES

H.R. Rep. No. 1752, 95th Cong., 2d Sess., *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983 ..... 9, 13
Note, *Legislative History of the Natural Gas Policy Act: Title I*, 59 Tex. L. Rev. 101 (1980) 18
Committee Report on H.B. 2680, Kansas Journal of the House 962 (1978) 20
Rules of the Supreme Court of the United States, Rule 17.1(c) 1

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

No. 84——

PENNZOIL COMPANY,

Petitioner,

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

Pennzoil Company (Pennzoil) petitions for a Writ of Certiorari to review a decision of the Supreme Court of Appeals of West Virginia affirming an Order issued by the Public Service Commission of West Virginia (PSC). The Supreme Court of Appeals has erroneously decided the scope and applicability of Section 602(a) of the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3432(a), in a manner that conflicts with the legislative history of the NGPA, conflicts with this Court's prior decisions regarding sales and transportation of natural gas in interstate commerce, and conflicts with the intent of this Court in a previous decision in a related case. Pennzoil submits that "special and important reasons," satisfying the criteria of Sup. Ct. R. 17.1(c), justify granting a Writ of Certiorari in this case.

OPINIONS AND ORDERS BELOW

The opinion of the Supreme Court of Appeals of West Virginia in *Pennzoil Co. v. Public Service Commission*, Appeal No. 16513, is unreported. That opinion is set forth in Appendix A.[1] The accompanying order of the

[1] Materials included as Appendices will be cited as "App. ——."

Supreme Court of Appeals, affirming the underlying Order of the PSC on the basis of the court's written opinion, is set forth in Appendix B. The Order of the PSC, dated August 10, 1984, is set forth in Appendix C.

JURISDICTION

The order of the Supreme Court of Appeals was entered on March 1, 1985. Pennzoil invokes the jurisdiction of this Court pursuant to 28 U.S.C. § 1257(3).

STATUTES INVOLVED

The decision of the Supreme Court of Appeals affirmed an order of the West Virginia PSC that interpreted and relied upon Section 602(a) of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. § 3432(a). Section 602(a) of the NGPA states:

> Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under Subchapter I of [the NGPA].[2]

STATEMENT OF THE CASE

A. Introduction.

This case presents a substantial question of federal law that will determine the means and scope of state regulation of wellhead natural gas prices under the NGPA. That question is whether Section 602(a) of the NGPA authorizes the states to establish maximum prices, at the wellhead, for "first sales" of natural gas occurring in interstate commerce.

In 1983, this Court reviewed a related dispute between Pennzoil and West Virginia, in which the issue presented by this case first arose. In *Pennzoil Co. v. Public Service Commission of West Virginia*,[3] this Court granted Penn-

---

[2] 15 U.S.C. § 3432(a). Section 602 is set forth in full in App. D.

[3] —— U.S. ——, 103 S. Ct. 3564 (1983). This Court's memorandum decision is set forth in App. E.

zoil's Petition for Certiorari in Docket No. 81-1672, and reviewed the decisions of the Supreme Court of Appeals of West Virginia and the West Virginia PSC in PSC Case No. 80-175-G-42T. In a memorandum decision, this Court vacated the decision of the West Virginia Supreme Court, and remanded the case for further consideration in light of the decision in *Public Service Commission of New York v. Mid-Louisiana Gas Co.*[4] The decision in *Mid-Louisiana* had disposed of the threshold issue presented in Pennzoil's case by deciding that the NGPA is applicable to gas produced by pipelines and distribution companies. However, Pennzoil had presented a second question, which was whether Section 602(a) of the NGPA authorized the PSC to set a price for Pennzoil's production lower than the NGPA price. The Court's memorandum decision did not expressly address that question.[5]

On remand, the West Virginia Supreme Court sent the case back to the PSC, which issued its order on remand approximately nine months later. The PSC's decision on remand reached the same result as the original decision, this time relying on Section 602(a) and simply restating the rationale it had presented previously to this Court, but which this Court had not directly addressed. Pennzoil appealed that order to the West Virginia Supreme Court of Appeals. On July 11, 1984, the West Virginia court upheld the PSC's order on remand, without issuing any opinion or explanation of its reasoning. On October 9, 1984 Pennzoil filed a second Petition for Certiorari, in Docket No. 84-569, challenging the West Virginia decisions after the remand from this Court, and presenting for review the issue of the applicability of Section 602(a) of the NGPA.

At the same time, however, Pennzoil was pursuing a new rate case in West Virginia, PSC Case No. 83-333-G-42T, in which the PSC again issued an order relying

---

[4] —— U.S. ——, 103 S. Ct. 3024 (1983).

[5] *See* App. E.

on Section 602(a) of the NGPA to deny Pennzoil's rate request. While Pennzoil's Petition in Docket No. 84-569, regarding the remand of the original rate case, was pending in this Court, Pennzoil filed in the Supreme Court of Appeals a petition for appeal of the PSC's decision in Case No. 83-333-G-42T. The West Virginia court agreed to allow full briefing and argument in that case on the identical question that was pending in this Court on Pennzoil's Petition for Certiorari in Docket No. 84-569.[6]

In this Court, the PSC opposed Pennzoil's Petition in Docket No. 84-569 on the ground, *inter alia*, that the decision of the West Virginia court denying Pennzoil's appeal of the order on remand in Case No. 80-175-G-42T was not appropriate for certiorari because it had been issued without any accompanying opinion or explanation of the court's reasoning. Pennzoil responded by informing this Court that PSC Case No. 83-333-G-42T, presenting the same issue, was pending before the Supreme Court of Appeals, and that the West Virginia court had allowed a full appeal and would likely write a full opinion addressing the question of the applicability of Section 602(a) of the NGPA. Pennzoil suggested that if this Court desired a full explanation of the West Virginia court's reasoning, it could hold Pennzoil's Petition in abeyance, pending the expected opinion of the West Virginia court in the appeal in Case No. 83-333-G-42T on the same question. Instead, this Court subsequently chose to deny Pennzoil's Petition for Certiorari in Docket No. 84-569.[7]

Pennzoil proceeded with its appeal in PSC Case No. 83-333-G-42T before the West Virginia court, and that court ultimately rendered its opinion affirming the PSC. It is that final written opinion disposing of Case No. 83-333-G-42T which Pennzoil now requests this Court

---

[6] *See* App. F.

[7] 105 S. Ct. 566 (1984).

to review. For the first time in these related cases, the West Virginia court has written an opinion explaining its reasoning in upholding the PSC. The key flaw in the West Virginia court's opinion is that it essentially ignores the legal significance of the fact that the "first sale" of Pennzoil's production takes place in *interstate* commerce, and is thus beyond the power of the PSC to regulate, under any interpretation of Section 602(a) of the NGPA.

B. Facts.

Pennzoil is a producer of oil and natural gas operating approximately 2,200 wells that produce gas in West Virginia. In West Virginia, Pennzoil also purchases and resells gas from approximately 140 other independent producers. To transport its own gas and gas purchased from other producers from the wellhead to interstate pipeline customers, Pennzoil operates a gas gathering system. At any given time, approximately 60 percent of the gas in the gathering system has been produced by Pennzoil and approximately 40 percent has been purchased by Pennzoil from independent producers close to Pennzoil's gathering lines.

Pennzoil's primary business objective with respect to its gas production in West Virginia is to sell that gas to several interstate pipelines. On an average day, however, Pennzoil sells only about 75 percent of the gas it transports in its gathering system to interstate pipelines. The remainder is sold pursuant to West Virginia law and certain orders of the PSC, which require Pennzoil to sell gas on request to retail customers, if they are located near Pennzoil's gathering lines. Pennzoil performs this distribution-type service through a separate division, the Utility Division of Pennzoil Company. The respective volumes that will be sold to interstate pipelines and to retail customers on any given day cannot be predicted in advance, because they depend on the gas demands of the retail customers.

For the convenience of the Court, a diagram showing a representative schematic of Pennzoil's gas supply operations in West Virginia is set forth in Figure 1.

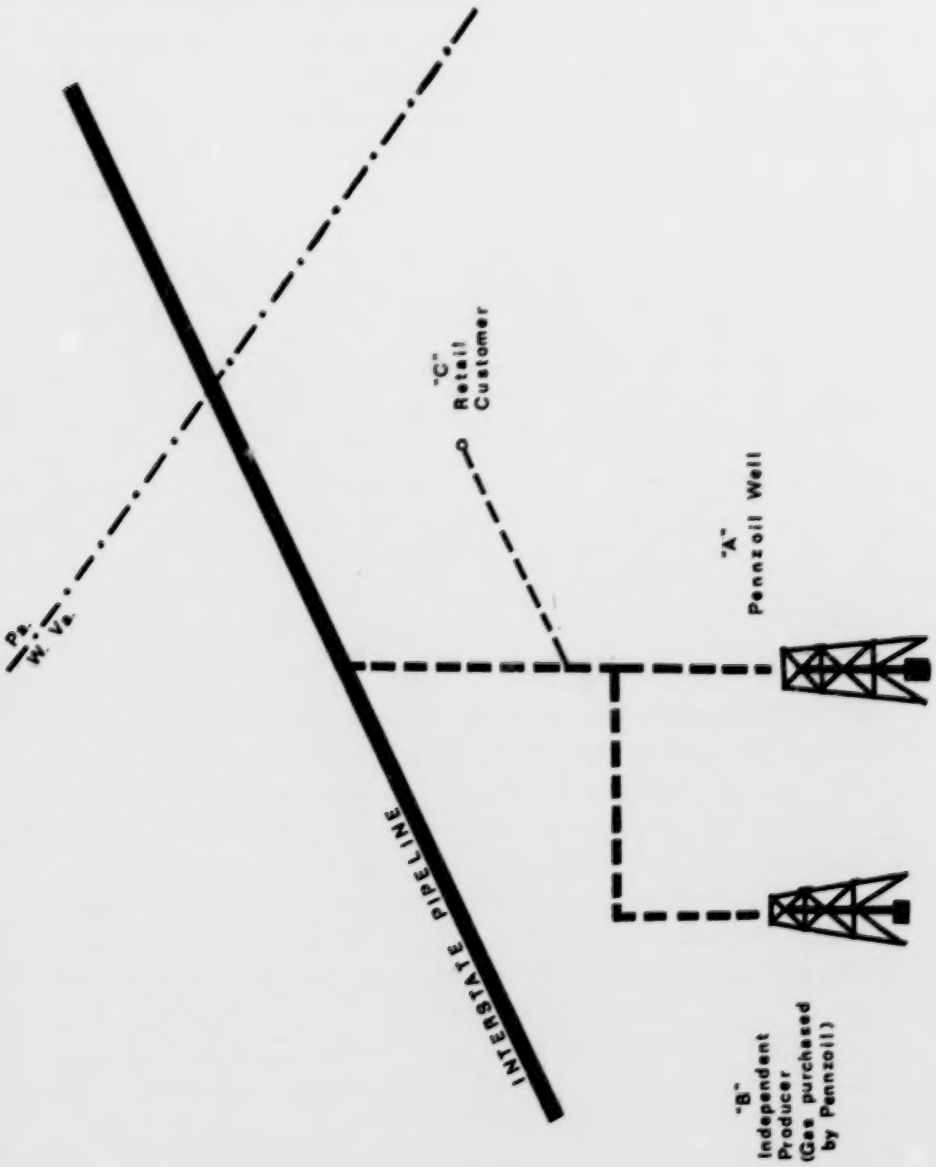

FIGURE 1

As illustrated in Figure 1, the gas to be supplied to a typical retail customer comes from the total gas supply flowing in Pennzoil's gathering system (represented by dashed lines). The total supply is made up of gas Pennzoil produces (at point "A") and gas Pennzoil purchases (at point "B"). If the retail customer (at point "C") has no need for gas at a particular moment in time, then all of Pennzoil's production flows to the interstate pipeline (represented by the solid line). On the other hand, if the retail customer turns on his stove or furnace at a particular moment, the small volume that customer burns is diverted from the stream of gas ultimately sold to the interstate pipeline. Until the gas actually leaves Pennzoil's gathering facilities and is burned by the retail customer, it remains part of the overall stream of gas flowing to the interstate pipeline.

Pennzoil's sales of gas to interstate pipelines are subject to federal price regulation because they are sales to the pipelines for resale to others, and because they take place "in interstate commerce."[8] Pennzoil's contracts with interstate pipelines are regulated by the Federal Energy Regulatory Commission (FERC) and not by the State of West Virginia.[9] Under those contracts, Pennzoil receives the applicable NGPA price for the gas Pennzoil sells to interstate pipelines.

In contrast, the retail sales of gas by Pennzoil's Utility Division, to customers required to be served under West Virginia law, are regulated by the PSC. Under the West Virginia Public Service Law,[10] the PSC has authority to regulate only the retail rate at the point where Pennz-

---

[8] 15 U.S.C. § 717(b).

[9] In FERC Docket No. G-7004, the FERC has required Pennzoil to obtain abandonment approval under Section 7(b) of the Natural Gas Act, 15 U.S.C. § 717f(b), before diverting any gas from sales to interstate pipelines for sale to West Virginia customers.

[10] W. Va. Code Chapter 24 (Supp. 1984).

oil's gas is actually sold to a West Virginia customer, represented as point "C" in Figure 1. The PSC has no authority to regulate the price of gas at the wellhead, represented as points "A" and "B" in Figure 1, because, as explained in Parts D and E *infra*, the wellhead price is set by the NGPA. The PSC sets the Utility Division's rates to retail customers on the basis of a "cost of service" ratemaking methodology, which requires a calculation of the Utility Division's gas costs, taxes, administrative expenses and other factors.[11] The major component of this cost of service calculation is the cost of "purchased gas," which includes both the actual cost of gas the Utility Division purchases from independent producers and the imputed "cost," or value, of gas produced by Pennzoil and subsequently transferred to the Utility Division for sale to West Virginia customers.

The Utility Division calculates its cost of the gas it purchases from independent producers on the basis of the price it actually pays to those producers, which, in the majority of Pennzoil's contracts, is the applicable NGPA price. Similarly, in calculating the "cost" of gas Pennzoil itself produces rather than purchases, the Utility Division assigns a value to Pennzoil's own production equivalent to the applicable NGPA price. The NGPA price accurately establishes the "cost" of Pennzoil's production, in terms of "opportunity cost," because that is the price Pennzoil receives if it sells its gas production to interstate pipelines.

The dispute in this case arises because the PSC has denied that the wellhead prices established by the NGPA are a reasonable measure of the "cost," to the Utility Division, of Pennzoil's own gas production, and relying on a mistaken interpretation of Section 602(a) of the NGPA, has refused to utilize those prices in determining the Utility Division's cost of service to West Virginia retail customers. The West Virginia Supreme Court has

---

[11] W. Va. Code § 24-1-1(a)(4) (Supp. 1984).

accepted the PSC's rationale, incorrectly distinguishing the prior decisions of this Court and ignoring the changes in natural gas regulation required by the NGPA.

C. The Provision Of The NGPA At Issue.

The NGPA extended federal price ceilings to intrastate sales of natural gas, and thus displaced state jurisdiction to regulate wellhead prices.[12] In Section 602(a) of the NGPA, however, Congress ceded back some authority to the states and defined the limited circumstances in which the states may override the uniform application of the maximum lawful prices established by the NGPA.

The chief prerequisite for state regulation, that the sale occur "in intrastate commerce," is specified in the Conference Report, which includes the following explanation of Section 602(a):

> The conference agreement provides that nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for sales of gas *in intrastate commerce* which does not exceed the applicable maximum lawful price, if any, under Title I of this Act. This authority extends to the operation of any indefinite price escalator clause. The Congress enacts this provision with a recognition that it is ceding its authority under the commerce clause of the Constitution to regulate prices for such production to affected States.[13]

---

[12] *See generally* Public Service Comm'n of New York v. Mid-Louisiana Gas Co., 103 S. Ct. 3024, 3029-34 (1983); Exxon Corp. v. Eagerton, 103 S. Ct. 2296 (1983); Energy Reserves Group v. Kansas Power & Light Co., 459 U.S. 400, 103 S. Ct. 697 (1983); Maryland v. Louisiana, 451 U.S. 725, 101 S. Ct. 2114 (1981); Oklahoma v. FERC, 494 F. Supp. 636 (W.D. Okla. 1980), *aff'd*, 661 F.2d 832 (10th Cir. 1981), *cert. denied, sub nom.* Texas v. FERC, 457 U.S. 1105 (1982). (Upholding the constitutionality of NGPA provisions extending federal price controls to intrastate sales of gas).

[13] H.R. Rep. No. 1752, 95th Cong., 2d Sess. 124-25, *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983, 9041 (emphasis added).

If the "first sale" occurs in *intrastate* commerce, and if a state has properly established maximum lawful prices for "first sales" pursuant to the authority granted by Section 602(a), then those prices may supplant the applicable NGPA prices. It is important to note that Section 602 only applies to *first* sales, and not other sales, and that it only applies to first sales that occur in *intrastate* commerce. In this case, the West Virginia court incorrectly based its decision on an assumption that the "first sale" of Pennzoil's production occurs in intrastate commerce.[14]

D. The Decision of This Court in Mid-Louisiana.

In *Public Service Commission of New York v. Mid-Louisiana Gas Co.*,[15] this Court held that Section 2(21) of the NGPA, 15 U.S.C. § 3301(21), required the application of NGPA prices to natural gas produced by interstate pipelines.[16] Due to the express inclusion of local distribution companies in the controlling language of Section 2(21), the Court's holding also established the applicability of NGPA prices to gas produced by local distribution companies such as Pennzoil. This Court remanded the *Mid-Louisiana* case to the FERC for a determination of the point at which the "first sale" under Section 2(21) would be deemed to occur, which would establish the point at which the NGPA price attaches to pipeline and distributor production.[17] The Court recognized that the FERC could logically conclude that a "first sale" occurred either (a) at the "intracorporate transfer" point, where pipeline production is transferred from production facilities to transmission or distribution facilities; or (b) at the downstream point at which the gas is transferred to the end-user.[18]

---

[14] App. A at 7a-8a.

[15] 103 S. Ct. 3024 (1983).

[16] 103 S. Ct. at 3034-35.

[17] *Id.* at 3037.

[18] *Id.* at 3037.

E. The Effect of the FERC Final Rule Implementing Mid-Louisiana.

On August 22, 1984, the FERC issued its Order No. 391, which implements the decision in *Mid-Louisiana.*[19] In Order No. 391, the FERC established that the "first sale" of production by pipelines and distribution companies occurs at the "intracompany transfer point", which it defined as occurring at the wellhead.[20] In addition, after comments and testimony by Pennzoil, and after comments in opposition by the PSC, the FERC expressly decided that its definition of the point of "first sale" at the wellhead applies uniformly throughout the United States, to all gas produced by local distribution companies, such as Pennzoil, as well as to interstate pipelines.[21] The "point of first sale" is important because it establishes the point at which the NGPA applies, and establishes the initial "cost" or value, to the Utility Division, of Pennzoil's production.

The FERC final rule is critical to this case. Briefly, as explained below, the FERC's determination that the "first sale" occurs at the wellhead establishes that, in this case, the first sale occurs "in interstate commerce," because, at the wellhead, all of Pennzoil's production is in interstate commerce. That means that the price for Pennzoil's production in that "first sale" is beyond the power of the PSC to regulate under Section 602(a) of the NGPA, because Section 602(a) is not applicable to first sales that occur in interstate commerce. As a result, the price for Pennzoil's gas in the intracorporate

---

[19] 49 Fed. Reg. 33,849 (Aug. 27, 1984). On August 29, 1984, the FERC issued minor corrections to portions of Order No. 391. Those corrections were published at 49 Fed. Reg. 39,293 (Oct. 5, 1984). The relevant portions of the regulations established in Order No. 391, as corrected by the FERC, are set forth in App. G.

[20] 49 Fed. Reg. 33,859 (1984), as corrected (to be codified at 18 C.F.R. § 270.203).

[21] 49 Fed. Reg. 33,856.

transfer from Pennzoil's production division to its Utility Division, at the wellhead, must be the NGPA price, and the PSC must use that price as the starting point in setting the downstream price in the Utility Division's subsequent sale to a West Virginia retail customer.[22]

REASONS FOR GRANTING THE WRIT

Pennzoil seeks a Writ of Certiorari to obtain review of West Virginia's unlawful application of Section 602 (a) of the NGPA to "first sales" that occur "in interstate commerce," in direct conflict with the legislative history of Section 602(a) and with this Court's prior decisions interpreting the Natural Gas Act and the Natural Gas Policy Act. That issue presents a substantial question of federal law, and is of nationwide impact and significance in establishing the dividing line between federal and state authority in regulating sales of natural gas.

A. Pennzoil's Production in West Virginia is Not Subject to Section 602(a) of the NGPA.

In Order No. 391, the FERC ruled that "[a] transfer, at the wellhead, of gas produced by a local distribution company's production unit is that company's first sale under the NGPA."[23] At the point of first sale, at the wellhead, any of Pennzoil's production that may be transferred to the Utility Division and ultimately delivered to West Virginia retail customers is mixed with and indistinguishable from Pennzoil's overall gas supply. Therefore, it is impossible to determine, at the wellhead, whether particular volumes of gas will be consumed by customers within West Virginia, or whether those vol-

---

[22] *See* Mid-Louisiana Gas Co. v. FERC, 664 F.2d 530, 537 (5th Cir. 1981), *vacated and remanded on other grounds sub nom.* Public Service Comm'n of New York v. Mid-Louisiana Gas Co., 103 S. Ct. 3024 (1983).

[23] New Section 270.203(b)(3) as corrected, 49 Fed. Reg. 39,293 (Oct. 5, 1984) (to be codified at 18 C.F.R. § 270.203(b)(3)).

umes will flow to other states, to be consumed by customers outside West Virginia. Indeed, until the gas actually flows out of Pennzoil's gathering facilities and is consumed by a West Virginia retail customer, it remains in the stream of interstate commerce, destined for sale to an interstate pipeline. Under the unambiguous and longstanding decisions of the U.S. Supreme Court and the U.S. Courts of Appeals, the mixed volumes of gas at the wellhead are said to be "commingled", and, *at that point*, the *entire* volume of Pennzoil's production is "in *interstate* commerce." [24]

The authorization granted by Congress in Section 602(a) of the NGPA allows the States to establish maximum lawful prices lower than the applicable NGPA prices, but only with respect to first sales of gas "in *intrastate* commerce." [25] Because FERC Order No. 391 establishes that the "first sale" of Pennzoil's production occurs at the wellhead, and because the entire volume of Pennzoil's production at that point is "in *interstate* commerce," the PSC has no power under Section 602(a) of the NGPA to regulate the price for Pennzoil's production in that "first sale" to Pennzoil's Utility Division. Rather, the PSC must use the NGPA price as the Utility Divi-

---

[24] California v. Lo-Vaca Gathering Co., 379 U.S. 366, 369, 85 S. Ct. 486, 488 (1965) ("The fact that a substantial part of the gas will be resold [outside the state] in our view invokes federal jurisdiction at the outset over the entire transaction"); FPC v. Amerada Petroleum Corp., 379 U.S. 687, 689-90, 85 S. Ct. 632, 634, (1965); Louisiana Public Service Comm'n v. FPC, 359 F.2d 525, 528 (5th Cir.), *cert. denied*, 385 U.S. 833 (1966) ("[T]he mixing of intrastate gas with a substantial portion of interstate gas for pipeline transportation in one commingled stream" invokes federal jurisdiction); Deep South Oil Co. v. FPC, 247 F.2d 882 (5th Cir. 1957), *cert. denied*, 355 U.S. 930 (sale at wellhead takes place in interstate commerce where some of the gas ultimately is sold interstate and some intrastate) (1958).

[25] H.R. Rep. No. 1752, 96th Cong., 2d Sess. 124 *reprinted in* 1978 U.S. Code Cong. & Ad. News 8983, 9041 (emphasis added).

sion's acquisition cost of gas transferred to it in the "first sale" and must set the rate for the Utility Division's subsequent sales to West Virginia retail customers using that acquisition cost as a starting point.

In a factual situation similar to the situation presented by this case, the U.S. Court of Appeals for the Sixth Circuit summarized the federal law relating to the "commingling" doctrine, which determines whether, at the point of first sale, the gas is in interstate commerce.[26] The Sixth Circuit found that commingled volumes of gas were in interstate commerce, because the "ultimate sale in other states of a substantial part of a producer's natural gas output invokes federal jurisdiction over the entire volume of production." [27]

In Pennzoil's case, because the majority of Pennzoil's production is sold to interstate pipelines for resale outside the state, the entire volume of that producion is "in *interstate* commerce" at the wellhead, at the point of "first sale." In its opinion in this case, the West Virginia court conducted a superficial, and incorrect, analysis of the "commingling" cases and simply assumed away the applicability of the commingling doctrine.[28] The West Virginia court also assumed that this Court's decision in *Exxon Corp. v. Eagerton* [29] dealt with a commingling situation, despite the fact that there is no indication whatsoever in the *Exxon* opinion that the interstate and intrastate sales described therein were made from a single

---

[26] Public Service Commission of Kentucky v. FERC, 610 F.2d 439, 444 (6th Cir. 1979). *See also* cases cited n.17 *supra*. The decisions discussing the "commingling" concept constitute the well-settled law determining when a particular volume of gas is "in interstate commerce." The fundamental principles established by those cases are unaffected by anything in the NGPA.

[27] 610 F.2d at 444.

[28] App. A at 7a-8a.

[29] —— U.S. ——, 103 S. Ct. 2296 (1983).

commingled stream rather than from separate wells.[30] If allowed to stand, the West Virginia court's decision will be in direct conflict with this Court's longstanding decisions establishing the commingling doctrine and will resurrect commerce clause issues heretofore thought to have been laid to rest long ago.

Because the "first sale" takes place at the wellhead, and because the gas at that point is in interstate commerce, the NGPA price attaches to all of Pennzoil's production at that point. Section 602(a) does not apply to first sales that occur in interstate commerce. Therefore, the PSC is bound to use the NGPA price applicable to the "first sale" in the transfer to the Utility Division as the starting point in establishing the Utility Division's retail rates. Under the NGPA, the PSC retains the power to apply the West Virginia Public Service Law in determining the extent to which the Utility Division will be permitted in its rates for subsequent *retail* sales, to recoup the additional costs of serving retail customers, such as administrative expenses, distribution expenses and taxes. However, because the *first* sale occurs in interstate commerce, the NGPA totally preempts the PSC's authority to alter the price applicable to the *first* sale, at the wellhead, and the PSC must use the applicable NGPA price as the "cost" to the Utility Division of obtaining Pennzoil's production in determining the "gas cost" component of the Utility Division's rates to West Virginia customers.

To paraphrase this Court in *Mid-Louisiana*:

> The NGPA is designed to preserve the [West Virginia] Commission's authority under [West Virginia law] to regulate natural gas sales from pipelines to their customers; however, it is designed to supplant

---

[30] App. A at 7a.

> the Commission's authority to establish rates for the wholesale market, the market consisting of so-called "first sales" of natural gas.
>
> 103 S. Ct. at 3031.

In this case, the "wholesale market" is the "first sale" transfer from Pennzoil's production facilities to the Utility Division.

In *Mid-Louisiana Gas Co. v. FERC*,[31] the U.S. Court of Appeals for the Fifth Circuit addressed precisely this point. With respect to state regulation of *retail* sales, the Fifth Circuit stated:

> [I]f the NGPA prices attached to the intracorporate transfer by the producer then the state's jurisdiction over retail sales would remain intact. The only change would be that the cost of the gas to the pipeline or distribution company would be the NGPA price. Jurisdiction to set the final retail charge would remain with the state. *Although the retail price would reflect the NGPA cost of gas*, that change is consistent with Congress' desire to establish a uniform price for producers of both intrastate and interstate gas.[32]

In light of the Fifth Circuit's interpretation of the intent of Congress in exactly the situation in this case, and in light of FERC Order No. 391 clarifying that the "first sale" does occur at the intracorporate transfer point, exactly as the Fifth Circuit assumed, there can be no doubt that the PSC is required to use the applicable NGPA price as the starting point in calculating the Utility Division's cost of gas service to West Virginia customers.

---

[31] 664 F.2d 530 (5th Cir. 1981), *vacated and remanded on other grounds sub nom.* Public Service Comm'n of New York v. Mid-Louisiana Gas Co., 103 S. Ct. 3024 (1983).

[32] 664 F.2d at 537 (emphasis added).

B. The West Virginia Legislature Has Chosen Not To Exercise Its Authority Under Section 602.

Even if, contrary to fact and law, none of Pennzoil's production ever were sold to interstate pipelines, and the "first sale" of that gas were in intrastate commerce, the PSC still would have no power to set the wellhead price for Pennzoil's production. In Section 602(a), Congress ceded its power to regulate prices for first sales in intrastate commerce to the "States" and not to state agencies. The NGPA contains a precise definition of the term "State", which does not include any reference to state agencies.[33] In other sections of the NGPA, Congress delegated powers to state jurisdictional agencies by explicitly referring to the agency itself, and not by using the term "State." [34] In view of the NGPA's specific definition of the term "State," the delegation of authority in Section 602(a) must be viewed as a delegation to state legislatures rather than to state agencies. Therefore, the PSC has no power to implement Section 602(a) unless that power has been properly delegated to the PSC by the West Virginia Legislature.

The opinion of the West Virginia court in this case ignores the intent of Congress evidenced by the overall scheme of the NGPA and ignores the fact that the NGPA was intended to change the historical cost-based methods of regulating "first sale" prices in the United States. In West Virginia, the Legislature has chosen not to enact any statute establishing maximum lawful prices for "first sales" in intrastate commerce. Further, the Legislature has chosen not to delegate any authority to the PSC to regulate wellhead sales under Section 602(a) of the NGPA.[35] Therefore, the PSC has no power under Section

---

[33] The NGPA defines the term "state" as "each of the several States and the District of Columbia." 15 U.S.C. § 3301(34).

[34] *See, e.g.*, § 503, 15 U.S.C. § 3413.

[35] The Legislature has stated that "the Commission shall carry out other federal acts, including appropriate portions of the 'Natural

602(a) of the NGPA to regulate the "first sale" price for Pennzoil's production. The West Virginia court totally disregarded this lack of statutory authorization for the PSC's actions.[36]

C. Section 602(a) Precludes Establishment Of Rates On A Case-By-Case Basis.

Finally, even if it is somehow deemed to have authority to set wellhead prices, the PSC has no power under Section 602(a) of the NGPA to regulate the "first sale" price for Pennzoil's production on a case-by-case basis in a retail rate proceeding. If Congress had intended to allow the states to set "first sale" prices in individual cases, using a "cost of service" methodology, it would have expressly said that the states could set "just and reasonable" prices, rather than "maximum lawful" prices.

In Section 602(a) of the NGPA, Congress authorized the states to set "maximum lawful" prices lower than the applicable maximum prices established by the NGPA.[37] Before the NGPA, under the Natural Gas Act, the FERC had established "just and reasonable" prices for producer sales of natural gas in interstate commerce relying primarily on a cost of service ratemaking methodology. The NGPA concept of "maximum lawful price" was intended to replace the cost-based "just and reasonable" prices that had existed under the Natural Gas Act, with uniform statutory prices based in large part on the level of incentive Congress deemed necessary to elicit new gas supplies.[38]

Gas Policy Act of 1978,' for which the governor designates it as the responsible agency in this State." W. Va. Code § 24-2-13. The Governor of West Virginia has not designated the PSC as the responsible agency for any purposes under the NGPA.

[36] App. A at 8a-10a.

[37] 15 U.S.C. § 3432(a).

[38] *See generally* Note, *Legislative History of the Natural Gas Policy Act: Title I*, 59 Tex. L. Rev. 101, 106-21 (1980) for an expla-

In the NGPA, Congress put an end to "cost of service" ratemaking for producers of natural gas at the federal level by establishing categories of uniform "maximum lawful prices" applicable to all "first sales" of gas in the United States. Thus, when it used the term "maximum lawful price" in Section 602(a), Congress intended only to authorize the states to establish generally applicable categories of ceiling prices for "first sales" in intrastate commerce.[39] In *Mid-Louisiana*, this Court implicitly adopted that interpretation, stating that Section 602(a) "allows the states to establish *price ceilings* . . . lower than the *federal ceiling*." [40]

In West Virginia, the Legislature may enact a statutory plan of uniform maximum lawful price ceilings under the authority of Section 602(a), or it may, by statute, delegate to the PSC the authority to establish uniform maximum prices for all producers by regulation. In no circumstance, however, does the PSC have the power to implement Section 602(a) on a case-by-case basis, effectively setting wellhead prices only for some producers, who happen also to perform a public service by selling a portion of their gas to retail customers.

When it enacted Section 602(a), Congress must have been aware of the existence of the New Mexico Natural Gas Pricing Act, which had been enacted by the New

---

nation of the cost-based "just and reasonable" ratemaking methodology under the Natural Gas Act and a comparison with the system of maximum lawful prices established by the NGPA.

[39] Congress used the term "maximum lawful price" throughout the NGPA when referring to the general categories of prices applicable to all "first sales" of gas.

[40] 103 S. Ct. 3024, 3036 n.20 (emphasis added). *See also* Exxon Corp. v. Eagerton, 103 S. Ct. 2296, 2203 (1983) (States may "establish *a price ceiling* for intrastate producer sales of gas at a level lower than the federal ceiling.") (emphasis added).

Mexico Legislature in 1977.[41] In that statute, New Mexico established a ceiling price for all sales of gas produced in New Mexico and sold in intrastate commerce, subject to certain limitations and escalations.[42] Since the effective date of Section 602, two states have joined New Mexico in enacting statutes establishing maximum lawful prices for sales in intrastate commerce.[43] The only logical construction of Section 602(a) is that Congress intended to allow the states to exercise their authority in the same fashion as New Mexico, establishing uniform ceiling prices by statute.

Finally, Congress could not have intended to give the states power to discriminate by using Section 602 on an ad hoc basis, purely as a means of reducing the rate a particular company may charge. If the PSC in fact has any authority under Section 602(a), it must exercise that authority uniformly, on a statewide basis, establishing a set of maximum lawful prices applicable to every producer in West Virginia. The incongruity of the Commission's position in this case is apparent from the fact that the PSC has made no effort whatsoever to prevent non-utility producers of natural gas in West Virginia from collecting the applicable NGPA price.

D. Potential Consequences Of The Commission's Assertion Of Authority.

The PSC's assertion of authority to set wellhead prices under Section 602(a) is based on a "business as usual"

---

[41] N.M. Stat. Ann., §§ 62-7-1 to 62-7-10 (1978). Senator Domenici of New Mexico was one of the nine Managers of the Conference on the NGPA on the part of the Senate.

[42] *See* Hecht Co. v. Southern Union Co., 474 F. Supp. 1022, 1029-30 (D.N.M. 1979).

[43] Kansas Natural Gas Price Protection Act, Kan. Stat. Ann. §§ 55-1401 to 1415 (Supp. 1980); Oklahoma Natural Gas Price Protection Act, 52 Okla. Stat. Ann. §§ 260.1 to 260.13 (Supp. 1980). The legislative history of the Kansas Act specifically references the authority granted to the states by the NGPA. Committee Report on H.B. 2680, Kansas Journal of the House at 962 (1979).

approach that ignores the changes in wellhead price regulation enacted by Congress in the NGPA. The decision of the Supreme Court of Appeals upholding the Commission's action suffers from the same analytical blindspot. Unless this error is corrected, the purposes of the NGPA will be seriously undermined. In addition, the PSC's usurpation of authority to lower the wellhead prices set by the NGPA will have significant practical consequences for all producers of natural gas in West Virginia and in other states that follow West Virginia's example.

The interpretation of Section 602(a) adopted by the PSC would allow state public service commissions to regulate wellhead gas prices without authorization from their state legislatures. Nothing in the provisions or history of the NGPA suggests in any way that Congress intended Section 602(a) to authorize state commissions to regulate wellhead prices without state statutory authorization. In addition, if state public service commissions may establish the maximum lawful prices referred to in Section 602(a) on a case-by-case, cost-of-service basis, there will be as many "maximum lawful prices" as there are wells within the state. Production from each well could receive a different cost-based price, depending on the particular circumstances of that well.

In West Virginia alone, the burden of case-by-case regulation of "first sales" in intrastate commerce would be enormous. In West Virginia, there presently exist more than 46,000 producing oil and gas wells from which sales of gas are or may someday be made. In addition to the regulatory burden the PSC's interpretation would impose on West Virginia producers, the PSC itself would be faced with the immense task of conducting cost-of-service rate proceedings for every individual producer sale and establishing a "maximum lawful rate" for each of those sales. Every producer rate decision would be subject to judicial review.

In summary, the interpretation adopted by the PSC and upheld by the Supreme Court of Appeals would begin anew the same type of revolution in natural gas price regulation in the states that this Court's decision in *Phillips Petroleum Co. v. Wisconsin* [44] began at the federal level. In view of the long experience, and extreme difficulty, of the Federal Power Commission in implementing the *Phillips* decision through case-by-case producer price regulation,[45] and in view of the fact that one of the purposes of the NGPA was to relieve that difficulty by eliminating cost-based regulation of producer prices, the PSC's interpretation requiring case-by-case, cost-of-service regulation of "first sales" cannot be correct. As this Court held in *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, "Congress explicitly envisioned that the states would regulate intrastate markets in accordance with the overall national policy." [46] The PSC's case-by-case approach to producer pricing is contrary to national policy, as enunciated by Congress in the NGPA, and must be struck down.

CONCLUSION

The questions presented by this case are of national importance, affecting every producer of gas making sales at wholesale and retail, and affecting the powers and duties of every state legislature and state regulatory commission. In essence, the West Virginia court has authorized the PSC to regulate not only retail sales, but to reach back to the "first sale," at wholesale, and regulate that price as well, even where that first sale occurs while all the gas is in interstate commerce. Unless this Court resolves the questions presented, the proper appli-

---

[44] 347 U.S. 672 (1954).

[45] *See In re* Permian Basin Area Rate Cases, 390 U.S. 747, 755-58 (1968).

[46] 459 U.S. 400, 420-21, 103 S. Ct. 697, 710 (1983).

cation of the NGPA to thousands of transactions nationwide will be uncertain. Therefore, Pennzoil respectfully requests this Court to grant a Writ of Certiorari.

Respectfully submitted,

/s/ Bruce F. Kiely
BRUCE F. KIELY
Counsel of Record
KIRK K. VAN TINE
BAKER & BOTTS
1701 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 457-5500
Attorneys for Petitioner Pennzoil Company

Of Counsel:

JOHN B. CHAPMAN
PENNZOIL COMPANY
Post Office Box 2967
Houston, Texas 77001

C. E. GOODWIN
GOODWIN & GOODWIN
500 Church Street
Ripley, West Virginia 25271

Dated: May 29, 1985

APPENDICES

APPENDIX A

SUPREME COURT OF APPEALS OF WEST VIRGINIA

No. 16513

PENNZOIL COMPANY

v.

THE PUBLIC SERVICE COMMISSION,
THE CONSUMER ADVOCATE DIVISION OF
THE PUBLIC SERVICE COMMISSION

Appeal — Affirmed

No. 16572

PENNZOIL COMPANY

v.

THE PUBLIC SERVICE COMMISSION

Prohibition — Writ Denied

Miller, Justice

[Filed Mar. 1, 1985]

1. Under Section 602(a) of the Natural Gas Policy Act, 15 U.S.C. § 3432(a), a state may establish a price for an intrastate producer's sales of gas in intrastate commerce at a level lower than the federal ceiling set by the Natural Gas Policy Act, 15 U.S.C. § 3301, *et seq.*

2. Congress did not intend by using the word "States" in Section 602(a) of the Natural Gas Policy Act, 15

U.S.C. § 3432(a), to change the historic method that state legislatures have handled the intrastate regulation of public utilities, which is by legislatively created utility commissions.

3. "Where an agency has been granted broad regulatory authority, it is not obligated to employ any single formula or combination of formulas to determine what in each case are just and reasonable rates." Syllabus Point 6, *Chesapeake and Potomac Tel. Co. of West Virginia v. Public Serv. Comm'n*, —— W. Va. ——, 300 S.E.2d 607 (1982).

Miller, Justice:

The Pennzoil Company claims it is aggrieved by a final order of the Public Service Commission (PSC), holding that the PSC has authority to set the price of that portion of Pennzoil's West Virginia gas production which is sold to retail consumers in this State. Part of Pennzoil's production is transmitted in interstate commerce, but the PSC does not claim jurisdiction to set prices for this gas.

Pennzoil argues that as a result of a recent United States Supreme Court opinion, *Public Serv. Comm'n of New York v. Mid-Louisiana Gas Co.*, —— U.S. ——, 77 L. Ed. 2d 668, 103 S. Ct. 3024 (1983), and an order by the Federal Energy Regulatory Commission (FERC), the PSC has no jurisdiction to set pricing guidelines for West Virginia gas production sold to West Virginia retail customers. Pennzoil claims that under *Mid-Louisiana* and the FERC order its gas price is controlled solely by the Natural Gas Policy Act, 15 U.S.C. § 3301, *et seq.* (1978) (NGPA). We disagree.

Mid-Louisiana did not involve an attempt on the part of a state to regulate the price of gas produced and sold to retail customers within its borders. In *Mid-Louisiana*, certain interstate pipeline companies complained that FERC, which is charged with issuing regu-

lations under the NGPA, had promulgated two regulations excluding them in certain instances from the benefit of the higher prices available under the NGPA.

The United States Supreme Court concluded that FERC had too narrowly construed the coverage of the NGPA in excluding the pipeline companies from its benefits. The Court directed FERC to establish at what point the interstate pipeline company could get the benefit of the NGPA rates:

> "The Commission's position is contrary to the history, structure, and basic philosophy of the NGPA. Like the Court of Appeals, we conclude that its exclusion of pipeline production is 'inconsistent with the statutory mandate [and would] frustrate the policy that Congress sought to implement.' *Federal Election Commission v. Democratic Senatorial Campaign Committee*, 454 U.S. 27, 32, 70 L. Ed. 2d 23, 102 S. Ct. 38 (1981). Unlike the Court of Appeals, however, we believe Congress intended to give the Commission discretion in deciding whether first sale treatment should be provided at the intracorporate transfer or at the downstream transfer." —— U.S. at ——, 77 L. Ed. 2d at 686, 103 S. Ct. at 3037. (Footnote omitted).

It is clear from *Mid-Louisiana*'s historical survey of the developments leading to the passage of the NGPA that one of the problems contributing to the natural gas shortage on the interstate level was low federal rates. Federal regulation of interstate rates through the Natural Gas Act, 15 U.S.C. § 717, *et seq.*, kept these rates considerably below the intrastate rates which were not under federal regulation. This caused shortages in the supply of interstate gas in the early 1970's, because gas producers and distributors saved their gas for the more lucrative intrastate market. As the United States Supreme Court noted in *Mid-Louisiana*: "The interstate

rates remained substantially below the unregulated prices available for intrastate sales, and the interstate supply remained inadequate." —— U.S. at ——, 77 L. Ed. 2d at 678, 103 S. Ct. at 3031. *See also* Breyer and Mac Avoy, *The Natural Gas Shortage and the Regulation of Natural Gas Producers*, 86 Harv. L. Rev. 941, 965-79 (1973); Note, *Legislative History of the Natural Gas Policy Act: Title I*, 59 Texas L. Rev. 101, 112 (1980).

We conclude from this historical discussion that one of the chief reasons for the adoption of the NGPA was to encourage producers to sell their gas on the interstate market by ensuring that a higher price did not exist in the intrastate market.[1] In order to achieve this result, pricing parity for what the NGPA termed "first sales" was mandated in the interstate and intrastate markets, Sections 104 and 105, 15 U.S.C. §§ 3314, 3315, subject to an important qualification contained in Section 602(a) of the NGPA, 15 U.S.C. § 3432(a): "*Authority to prescribe lower maximum lawful prices.*—Nothing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this chapter."

This language clearly allows states to set a *lower* price for intrastate sales than that mandated under the NGPA. Obviously, a lower intrastate price is consistent with one of the aims of the NGPA, preventing the intrastate price from going above the interstate price. *Mid-Louisiana* recognized the effect of Section 602(a) in note 20:

---

[1] The United States Supreme Court in *Mid-Louisiana* noted that another policy behind the NGPA was "the establishment of a statutory incentive price structure that would simultaneously promote production and reduce the regulatory burden." —— U.S. at ——, 77 L. Ed. 2d at 679, 103 S. Ct. at 3031.

"As we recently noted in *Exxon Corp. v. Eggerton*, —— U.S. ——, ——, 76 L. Ed. 2d 497, 103 S. Ct. [2296] (1983), § 105(a) of the NGPA extends federal authority to control producer prices to the intrastate market, but at the same time § 602(a) allows the States to establish the price ceilings for that market that are lower than the federal ceiling." —— U.S. at ——, 77 L. Ed. 2d at 685, 103 S. Ct. at 3036.

This point was forcefully made in *Exxon Corp. v. Eggerton*, —— U.S. ——, 76 L. Ed. 2d 497, 103 S. Ct. 2296 (1983), where Alabama had enacted a severance tax on oil and gas. By statute, it prohibited oil and gas producers from passing on the severance tax to purchasers through their prices. The United States Supreme Court held that the pass-through prohibition on sales of gas in interstate commerce was preempted under the NGPA and, therefore, invalid. However, the Supreme Court refused to invalidate the statute as to intrastate sales, stating:

"We reach a different conclusion with respect to the application of the pass-through prohibition to sales of gas in intrastate commerce. Although § 105 (a) of the NGPA extended federal authority to control prices to the intrastate market, 15 USC § 3315 (a) [15 USCS § 3315(a)], *Congress also provided that this extension of federal authority did not deprive the States of the power to establish a price ceiling for intrastate producer sales of gas at a level lower than the federal ceiling. Section 602(a) of the NGPA*, 15 USC § 3432(a) (Supp IV) [15 USCS § 3432(a)], states that

'[n]othing in this chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under subchapter I of this chapter.'"

—— U.S. at ——, 76 L. Ed. 2d at 507-08, 103 S. Ct. at 2303. (Emphasis added; footnote omitted).

If *Exxon* is not sufficiently clear, further support for our reading of Section 602(a) is found in *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, 459 U.S. 400, 74 L. Ed. 2d 569, 103 S. Ct. 697 (1983). There, Kansas had enacted a statute regulating the price of intrastate natural gas. One of the effects of the statute was to establish a price that was lower than the NGPA price. The utility argued in part that the state could not set a lower price than the NGPA, but the United States Supreme Court held that it could, finding this explicit language in the Conference Report on the NGPA:

> " 'The conference agreement provides that nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for sales of gas in intrastate commerce which does not exceed the applicable maximum lawful price, if any, under Title I of this Act. This authority extends to the operation of any indefinite price escalator clause.' S. Conf. Rep. No. 95-1126, pp 124-125 (1978); HR Rep. No. 95-1752, pp 124-125 (1978)." 459 U.S. at 417, 74 L. Ed. 2d at 584-85, 103 S. Ct. at 708.

Additionally, the Supreme Court stated in note 17: "The instant case does not raise a Commerce Clause issue because the parties agree that the gas is not in interstate commerce and because Congress, by § 602, authorized the State to regulate its price." 459 U.S. at 414, 74 L. Ed. 2d at 582, 103 S. Ct. at 706. We, therefore, conclude that under Section 602(a) of the NGPA, a state may establish a price for an intrastate producer's sale of gas in intrastate commerce at a level lower than the federal ceiling set by the NGPA.

Pennzoil argues that FERC's Order No. 391 issued on August 22, 1984, forecloses any further assertion of

jurisdiction by the PSC over pricing, but we again disagree. Clearly, FERC's order was issued in response to the Supreme Court's direction in *Mid-Louisiana* to establish whether the NGPA price should be applied "at the intracorporate transfer or the downstream transfer." —— U.S. at ——, 77 L. Ed. 2d at 686, 103 S. Ct. at 3037.[2] In its order, FERC chose the intracompany transfer point, defining it as the wellhead for purposes of applying the NGPA price. Its order had nothing to do with Section 602(a) of the NGPA.

Consequently, the FERC order does not answer the critical question in this case, which is whether Section 602(a) allows the PSC to set a lower price. We believe that both the language of Section 602(a) and the Supreme Court's treatment of this section in *Mid-Louisiana*, *Exxon* and *Energy Reserves* indicates that the PSC may do so for wholly intrastate sales of gas.

Moreover, *Exxon* appears to refute Pennzoil's argument that commingling of interstate and intrastate gas at the wellhead, the first point of sale for NGPA purposes, prevents separate pricing on the intrastate level, so that the NGPA price applies to all gas. The parties in *Exxon* stipulated "that a substantial portion of the gas extracted . . . was sold in interstate commerce." —— U.S. at —— n.6, 76 L. Ed. 2d at 357 n.6, 103 S. Ct. at 2303 n.6, yet, the Supreme Court had no difficulty in holding that the Alabama severance tax provision was valid as to the intrastate portion of production.

We do not believe that *California v. Lo-Vaca Gathering Co.*, 379 U.S. 366, 13 L. Ed. 2d 357, 85 S. Ct. 486 (1965), and *Federal Power Comm'n v. Amerada Petroleum Corp.*, 379 U.S. 687, 13 L. Ed. 2d 605, 85 S. Ct. 632 (1965), compel an opposite result. Both of these cases

---

[2] FERC acknowledged this on the first page of its Order No. 391 by stating: "This final rule implements the Supreme Court's decision in *Public Service Comm'n of New York v. Mid-Louisiana Gas Co.*, 103 S. Ct. 3024 (1983)."

involved the jurisdiction of the Federal Power Commission over sales of natural gas in which gas sold in intrastate commerce was commingled with interstate gas. The Supreme Court, relying on prior precedent interpreting the provisions of the Natural Gas Act, 15 U.S.C. § 717, *et seq.*, held that: "The result of our decisions is to make the sale of gas which crosses a state line at any stage of its movement from wellhead to ultimate consumption 'in interstate commerce' within the meaning of the Act." *Lo-Vaca*, 379 U.S. at 369, 13 L. Ed. 2d at 360, 85 S. Ct. at 488. We do not believe that this interpretation of the Natural Gas Act controls in the present case in view of Section 602(a) of the NGPA and the fact that the gas sought to be regulated in this case is wholly intrastate.

Pennzoil argues as a fall-back position that if Section 602(a) gives the State jurisdiction to set prices, this is a right given to the legislature and not to the PSC. This argument relies on the fact that Section 602(a) utilizes the term "States" which is defined in the NGPA as "each of the several States and the District of Columbia." Section 2(34); 15 U.S.C. § 3301(34). Pennzoil maintains that, as a consequence, only the legislature can act to establish prices, and asserts that our legislature has failed to do so since the enactment of the NGPA. Pennzoil also contends that such an intrastate pricing policy should be implemented by uniform rule rather than by case-by-case determination.

With regard to this argument, we believe that Section 602(a) embodied a congressional scheme under which the NGPA would set pricing for intrastate gas, without foreclosing the states from setting a lower price through their own regulatory agencies. Pennzoil does not cite any authority or point to anything in the legislative history of the NGPA suggesting that Congress intended by using the word "States" in Section 602(a) of the NGPA to change the historic method that state legislatures have

handled the intrastate regulation of public utilities, which is by legislatively created utility commissions.[3]

Furthermore, Pennzoil's argument that any price seting must be done by uniform rule rather than on a case-by-case basis was rejected on the federal level in *Lo-Vaca*. There the Supreme Court disposed of a similar argument with regard to the Federal Power Commission by stating that "we cannot say that the adjudicatory process is not an appropriate method for drawing the line case-by-case (United States v. Public Utilities Comm'n, 345 U.S. 295 [97 L. Ed. 1020, 73 S. Ct. 706 (1953)] as in a host of other administrative deliberations." 379 U.S. at 371, 13 L. Ed. 2d at 361, 85 S. Ct. at 489. We hereby reject this argument at the state level, if we have not already done so in Syllabus Point 6 of *Chesapeake and Potomac Tel. Co. of West Virginia v. Public Serv. Comm'n*, —— W. Va. ——, 300 S.E.2d 607 (1982), where we said:

> "Where an agency has been granted broad regulatory authority, it is not obligated to employ any single formula or combination of formulas to determine what in each case are just and reasonable rates."

The final argument posed by Pennzoil is that the PSC has no power to regulate wellhead prices under W. Va.

---

[3] There can be no question that the United States Supreme Court is well aware of state regulatory programs, as indicated by these remarks from notes 15 and 16 of *Energy Reserves*, 459 U.S. at 413, 74 L. Ed. 2d at 582, 103 S. Ct. at 706:

> "[15] In addition to the Kansas and federal regulations, 38 States regulate various aspects of gas production and sale. See Interstate Oil Compact Commission, Summary of State Statutes and Regulations for Oil and Gas Production (1979).
>
> "[16] For some time, the Court has recognized the validity of state regulation of the production and sale of natural gas in furtherance of conservation goals. . . . On several occasions, the Court has approved state price regulation of natural gas that did not interfere with interstate commerce." (Citations omitted)

Code, 24-2-1. In support of this position, Pennzoil cites *Eureka Pipe Line Co. v. Public Serv. Comm'n*, 148 W. Va. 674, 684, 137 S.E.2d 200, 206 (1964), a case which involved a question of the PSC's jurisdiction to regulate the marketing or production of oil. This Court found that the pipeline company was not serving members of the public and, therefore, was not a public utility. Here, there is no question that part of Pennzoil's gas is sold to members of the public; this is what brings it within the jurisdiction of the PSC. W. Va. Code, 24-2-1 and -3.[4]

It should be noted that this case is styled as a consolidated action. For the reasons stated in this opinion, we affirm the order of the PSC in Case No. 16513.

Case No. 16572 is an original writ of prohibition in which we issued both a rule to show cause against the PSC and a stay of further proceedings. This was done at the request of Pennzoil because it claimed that the PSC was proceeding in the underlying rate case to implement its gas pricing order. This order is the subject of the appeal in Case No. 16513. In view of the fact that we have determined that the PSC has jurisdiction to set pricing of gas produced and sold to retail customers in this State, so long as it does not exceed the NGPA price, we dismiss the rule to show cause in Case No. 16572.

No. 16513—Affirmed.

No. 16572—Writ denied.

---

[4] After this appeal was granted, we authorized a petition to intervene on behalf of the consumer advocate division of the PSC. In its brief, a cross-assignment of error is made which in effect challenges the PSC's methodology for setting Pennzoil's price below the NGPA price. The consumer advocate division agrees with the PSC that it has the jurisdiction to set a lower price, but believes the price should be lower than that set by the PSC. We decline to address this issue as it was not presented in the PSC hearing below. Furthermore, while intervention is permitted, under Rule 10(f) of our Rules of Appellate Procedure, cross-assignments of error are ordinarily limited to appellees.

APPENDIX B

STATE OF WEST VIRGINIA

At a Regular Term of the Supreme Court of Appeals continued and held at Charleston, Kanawha County, on the 1st day of March, 1985, the following order was made and entered, to-wit:

PENNZOIL COMPANY, a corporation,
Petitioner

16513 vs.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Respondent

ADVOCATE DIVISION OF PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Party Respondent

Upon an appeal from, suspension and review of an order of the Public Service Commission of West Virginia entered on August 10, 1984.

The Court having maturely considered the petition, the original record, the statement by respondent, Public Service Commission of West Virginia of its reasons for the entry of the aforesaid order, and the argument and briefs of counsel thereon, is of opinion for reasons stated in writing and filed with the record that there is no error in the order complained of. It is therefore considered and ordered by the Court that the order of the Public Service Commission entered in this proceeding on the 10th day of August, 1984, be, and it is hereby, affirmed;

all of which is ordered to be certified to the Public Service Commission.

It is further ordered that the Public Service Commission be, and it is hereby granted leave to withdraw the original papers, documents and evidence filed by it in this proceeding.

The syllabus of points adjudicated, prefixed to the written opinion prepared by Justice Miller, was concurred in by Chief Justice Neely and Justices McGraw, McHugh and Brotherton.

A True Copy

Attest: /s/ George W. Singleton
Clerk Supreme Court of Appeals

APPENDIX C

PUBLIC SERVICE COMMISSION
OF WEST VIRGINIA
CHARLESTON

At a session of the PUBLIC SERVICE COMMISSION OF WEST VIRGINIA at the Capitol in the City of Charleston on the 10th day of August, 1984.

Case No. 83-333-G-42T

PENNZOIL COMPANY, a corporation.
In the matter of increased
rates and charges

COMMISSION ORDER ON REMAND FROM THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

PROCEDURE

On July 11, 1983, Pennzoil Company, a corporation, filed for a $1.16 million rate increase which was suspended by the Commission until 12:01 a.m., March 12, 1984 to coincide with the temporary suspension of rate increases for natural gas utilities as prescribed by the legislature in *West Virginia Code* § 24-2B-1.

At a November 30, 1983 hearing Pennzoil and Staff submitted a Joint Stipulation and Agreement for Settlement of all issues other than produced gas costs which are to be allowed to Pennzoil. The hearing proceeded for the purpose of seeking approval of the proposed stipula-

tio as well as to receive evidence on the issue unresolved by Joint Stipulation.

On February 21, 1984, a Commission Hearing Examiner entered a decision approving the Joint Stipulation and resolving the remaining issues contained in the case. Exceptions to the Hearing Examiner's Decision were filed by Pennzoil on March 7, 1984.

The Commission affirmed the Hearing Examiner's Decision on March 9, 1984, noting that the issues in the exceptions required extensive review which could not be adequately performed within the time period required for a final order by the provisions of *Code* § 24-2-4 (as modified by *Code* § 24-2B-1). The failure of the Commission to enter a final order on or before March 12, 1984 would have resulted in the Company's rates taking effect as filed on March 12, 1984, and would constitute a neglect of duty on the part of the Commission. Since cursory review of the Hearing Examiner's Decision did not reveal any grievous error, the Commission affirmed the February 21, 1984 decision as a final order of the Commission. The Commission further provided that it would review the issues presented by the exceptions if the parties filed a petition for rehearing and reargument pursuant to Rule 19(c) of the Commission's *Rules of Practice and Procedure.*

On March 15, 1984, Pennzoil filed such a petition, asserting the same issues contained in its previous exceptions. That same day, Pennzoil filed a motion to place the rates as contained in its tariff sheets, filed on July 1, 1983, into effect subject to refund. Pennzoil's motion to place the originally requested rates into effect subject to refund was denied on March 29, 1984.

On April 5, 1984, Pennzoil filed a petition in the Supreme Court of Appeals of West Virginia (Court) seeking review of the case under *West Virginia Code* § 24-5-1, a stay of the Commission's March 9, 1984 order and

the authority to place its proposed rates into effect under bond. By order issued April 12, 1984, the Court set the petition for appeal for hearing, but denied Pennzoil's request for interim relief.

The Commission filed a motion with the Court requesting that the case be remanded to the Commission for reconsideration in light of the Commission's May 15, 1984 decision in *Pennzoil Company*, Case No. 80-175-G-42T, a case which addressed the identical issue presented by Pennzoil's appeal in this case. The Court granted the Commission's motion on July 11, 1984.

DISCUSSION

The remaining issue in this case concern [sic] the appropriate recovery rates to be included in Pennzoil's cost of service for its own gas production. Pennzoil contends that it should be permitted to include costs for its internal production which reflect the maximum lawful ceiling price for such gas under the Natural Gas Policy Act of 1978 (NGPA). If it is determined that NGPA ceiling rates are not appropriate, then the Commission must adopt a lawful alternate pricing methodology to establish a recovery rate for Pennzoil's self-produced gas.

In addressing this issue, the following questions were addressed by the Hearing Examiner's February 24 order:

> 1. What effect, if any, the recent United States Supreme Court decision in *Public Service Commission of the State of New York v. Mid-Louisiana Gas Co., et al.*, 103 S. Ct. 3024 (1983), has on Pennzoil's entitlement to price the gas it produces and sells to West Virginia ratepayers at the Natural Gas Policy Act of 1978 (NGPA) ceiling rates?
>
> 2. If Pennzoil is entitled to NGPA ceiling rates, does § 602 of the NGPA invoke this Commission with authority to price Pennzoil's gas at rates lower than the ceiling levels provided by the NGPA?

3. If NGPA ceiling rates are not appropriate for pricing Pennzoil's own Company production sold to West Virginia ratepayers, which cost of service pricing methodology (the Company BTU method or the Staff dry gas well method) is most appropriate for calculating the cost of Company produced gas?

The Hearing Examiner found that (HED, p. 7) the *Mid-Louisiana* case did not compel the Commission to price Pennzoil's produced gas at NGPA ceiling rates, but Pennzoil could price its gas at the ceilings absent state authority to establish lower rates (HED, pp. 11, 12). It was further determined that § 602 of the NGPA preserves the Commission's authority to price Pennzoil's produced gas sold to West Virginia consumers at rates lower than the NGPA ceiling levels. Upon review of the evidence, the Hearing Examiner found Staff's dry gas well proxy method of pricing Pennzoil's production gas from combination gas-oil wells was the most credible method of determining gas production costs that were contained in the record. (Conclusions of Law Nos. 5 and 20, HED, p. 27).

After the rendering of the Hearing Examiner's decision, which became a final order of the Commission on March 9, 1984, this Commission addressed similar issues pertaining to the establishment of an appropriate recovery rate for Pennzoil's own gas production in *Pennzoil Company*, Case No. 80-175-G-42T. We shall proceed to review the present case in light of this recent decision.

In Case No. 80-175-G-42T, we determined that as a result of the United States Supreme Court's decision in *Mid-Louisiana, supra*, this Commission is compelled to find that Pennzoil's own gas production in West Virginia, which is used for utility purposes, constitutes a first sale of gas under the provisions of the NGPA. However, even though this gas transaction constituted a first sale, we determined that Pennzoil was not neces-

sarily entitled to receive the maximum lawful price under the NGPA for the transaction. This determination was based on two key provisions of the NGPA.

We determined that under § 602(a) of the NGPA, the Commission maintains after the passage of NGPA the authority to establish a maximum lawful price for the first sale of Pennzoil's own gas production based on a cost of service pricing methodology. This section provides:

> § 602 EFFECT ON STATE LAWS.
>
> (a) Authority to prescribe lower maximum lawful prices.—Nothing in this Chapter shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under Title I of this Act.

Through the provisions of § 602(a) of the NGPA, Congress preserved the authority of the various States to establish maximum lawful prices for the first sale of natural gas which are lower that the ceiling prices established by the NGPA. Therefore, pursuant to the rate-making duties and authority bestowed on the Commission by the West Virginia Legislature through Chapter 24 of the West Virginia Code, we found that we had the authority to price Pennzoil's produced gas on a cost of service or other reasonable basis. (See May 15, 1984 order, Case No. 80-175, pp. 13-16).

Furthermore, we determined that even if § 602(a) of the NGPA did not apply, Pennzoil's intracorporate transfer of gas is not automatically entitled to the full maximum ceiling rate under the NGPA. Such automatic pricing would be contrary to the public interest for the same reasons noted by the United States Supreme Court in *Mid-Louisiana*, when it determined that "Congress undoubtedly intended pipeline producers to be treated in the same manner as pipeline affiliate producers" who are

"subjected to market control through the application of § 601(b)(1)(e)".[1] *Mid-Louisiana, supra,* at 3036. Therefore, just as the U.S. Supreme Court determined that an intracorporate transaction by an interstate pipeline is subject to the "affiliated entities test", so too did we determine that an intracorporate transaction by a local distribution company should be subject to a similar limitation. (See Case No. 80-175-G-42T, May 15, 1984, Commission Order, p. 16).

We determined that the Commission "has the authority under the NGPA to determine a just and reasonable price to be included in Pennzoil's rates for the recovery of its own production in West Virginia either by using a production cost of service study or by any other reasonable means, including a proxy for such cost of service." (Case No. 80-175-G-42T, May 15, 1984 Commission Order, pp. 15-16). In Case No. 80-175-G-42T, we concluded that there was insufficient evidence to establish an appropriate price for Pennzoil's internal production on the basis of a direct cost of service study. Therefore, we utilized a proxy for cost to determine a just and reasonable price for Pennzoil's own West Virginia gas production and priced Pennzoil's internal production in accordance with the wellhead prices paid by Pennzoil to its independent producers over the period in question, October 8, 1980 through October 13, 1982. (See Case No. 80-175-G-42T, May 15, 1984 Commission Order, pp. 17-18, Conclusion of Law No. 7. p. 21).

---

[1] NGPA § 601(b)(1)(e) provides as follows:

> (E) AFFILIATED ENTITIES LIMITATION—For purposes of paragraph (1), in the case of any first sale between interstate pipeline and any affiliate of such pipeline, any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

As noted in prior cases, the Commission has had great difficulty in calculating Pennzoil's cost of service associated with its gas production because much of the Company's production is derived from combination oil and gas wells. Therefore, the Commission has found it "very difficult, if not impossible, to separate the costs of oil and gas production," (Case No. 79-145-G-42T, Commission Order October 22, 1980, at p. 8). As noted on pages 16 through 18 of the Hearing Examiner's February 21, 1984 decision in this case, various efforts to make an adequate cost of service study have failed to provide a reasonable basis for deriving the costs associated with Pennzoil's West Virginia production. In the instant case, the parties have proposed two cost of service pricing methodologies.

Staff proposed a dry gas well method of calculating the Company's produced gas cost resulting in a proposed production gas cost of $3.26 per Mcf. (Staff Exh. No. 2, pp. 4-5). Since the Company actually keeps record of production costs in its dry gas fields, the Staff methodology uses these costs as a proxy for pricing the cost of gas from all Company wells, including those which produce produce [sic] both gas and oil. (Staff Exh. No. 2, pp. 4-5; Tr. 11/30/83, pp. 82, 87, 95).

Pennzoil proposed to allocate the costs of combination wells between gas production facilities and oil production facilities on the basis of the relative Btu content. (Pennzoil Exh. No. 4, p. 7). Application of Pennzoil's Btu content allocation factor would result in a cost of $5.44 per Mcf for the Company's produced gas cost.

We find it reasonable in this case to establish an appropriate rate for Pennzoil's own West Virginia production according to the methodology used in the Commission's May 15, 1984 remand order in Case No. 80-175-G-42T, which adopted the wellhead prices paid by Pennzoil to nonaffiliated producers as a proxy for cost. (See Conclusion of Law No. 7, Case No. 80-175-G-42T, May 15,

1984 Commission Order, at p. 21). In applying this method to the present case, we will continue to enforce a standard which is analogous to the "affiliated entities limitation" contained in § 601(b)(1)(E) of the NGPA. As noted in our May 15, 1984 order, we remain concerned that the continued practice of pricing Pennzoil's production according to nonaffiliated purchases may serve as a "disincentive to Pennzoil's efficient acquisition of the lowest cost nonaffiliated gas." (*Id.* at p. 18). However, we find that this concern is diminished in this case so long as the production period to be used as a proxy is sufficiently close in proximity to the May 15, 1984 order to ensure that the nonaffiliated purchase prices would not have been permitted to inappropriately escalate. Therefore, we believe that it is reasonable for the purposes of this case to price Pennzoil's production at a level which reflects the projected wellhead price paid by Pennzoil to nonaffiliated suppliers from March 12, 1984 through March 11, 1985, the first full year that rates established by this case shall be in effect. This calculated cost of production shall remain in effect until superseded by rate determinations made in subsequent cases. We will require Pennzoil to submit this calculated number to all parties, with supporting documentation, for review and eventual Commission approval. Since we will provide for Pennzoil's gathering cost at 86¢ per Mcf (See Staff Exh. No. 4 and Staff Exh. No. 5, Sheet 1 of 5) and production taxes at 8.63%, the producer prices utilized to derive this number should exclude any gathering allowance and production taxes.

In this case, the parties agreed to implement a special reduced rate schedule for Pennzoil's customers who are recipients of Social Security Supplemental Security Income (SSI) benefits (See HED, Appendix A, p. 8). This reduced rate schedule represents a portion of an experimental program instituted by this Commission to redistribute the burdens placed on certain low income cus-

tomers as a result of increasing utility costs. Since that time, a legislative program creating a twenty percent discount for eligible customers of gas and electric utilities during the winter heating season has been adopted and implemented. This program applies to Pennzoil's customers who are SSI recipients (See Senate Bill No. 110, amending *West Virginia Code* §§ 24-2A-1, *et seq.*, effective March 10, 1984). Since this legislative program establishes a methodology for the social redistribution of similar burdens, we believe that it is inappropriate to continue a selective experimental program that redistributes associated burdens in a manner which differs from the legislation. Therefore, we shall require Pennzoil to remove the special SSI rate schedule from its tariffs, effective upon the date of this order.

FINDINGS OF FACT

1. The Hearing Examiner's Decision of February 21, 1984 in this case, which became a Final Order of the Commission on March 9, 1984, determined that the Commission was not compelled to price Pennzoil's produced gas at NGPA ceiling rates, but Pennzoil could price its gas at the maximum lawful ceiling rate absent state authority to establish lower rates (HED pp. 11-12). The Hearing Examiner determined that such state authority existed and adopted Staff's dry gas well proxy method of pricing Pennzoil's production gas from combination gas-oil wells Conclusions of Law Nos. 5 and 20, HED, p. 27). On April 5, 1984, this decision was appealed to the West Virginia Supreme Court of Appeals.

2. In Case No. 80-175-G-42T, this Commission determined that the United States Supreme Court's decision in *Public Service Commission of the State of New York v. Mid-Louisiana Gas Co., et al.*, 103 S. Ct. 3024 (1983), compels this Commission to find that Pennzoil's own gas production in West Virginia, which is used for utility purposes, is entitled to treatment as a first sale of gas

under NGPA provisions. However, such treatment does not automatically entitle Pennzoil to receive the maximum law price under the NGPA for the transaction. (Commission Order on Remand, Case No. 80-175-G-42T, May 15, 1984).

3. Section 602(a) of the NGPA preserves the authority of the State to establish maximum lawful prices for the first sale of natural gas which are lower than the ceiling prices established by the NGPA. This Commission has determined that it therefore had the authority to price Pennzoil's produced gas on a cost of service or other reasonable basis pursuant to its statutory ratemaking authority (Commission Order on Remand, Case No. 80-175-G-42T, May 15, 1984).

4. In *Mid-Louisiana*, the United States Supreme Court determined that "Congress undoubtedly intended pipeline producers to be treated in the same manner as pipeline affiliate producers" who are "subjected to market control through the application of § 601(b)(1)(e)" of the NGPA. *Mid-Louisiana, supra*, at 3036. This Commission has determined that an intracorporate transaction by a local distribution company should be subject to similar scrutiny as an intracorporate transaction by an interstate pipeline, which is subject to an "affiliated entities test" under the *Mid-Louisiana* decision (Commission Order on Remand, Case No. 80-175-G-42T, May 15, 1984).

5. This Commission has previously determined that it "has the authority under the NGPA to determine a just and reasonable price to be included in Pennzoil's rates for the recovery of its own production in West Virginia either by using a production cost of service study or by any other reasonable means, including a proxy for such cost of service" (Commission Order on Remand, Case No. 80-175-G-42T, May 15, 1984, at pp. 15-16). In that case, this Commission proceeded to utilize a proxy for cost that was based on the wellhead prices paid by Pennzoil to its independent producers over a fixed period.

6. On July 11, 1984, the Supreme Court of Appeals of West Virginia remanded this case to the Commission for reconsideration in light of the Commission's May 15, 1984 decision in *Pennzoil Company*, Case No. 80-175-G-42T.

7. The stipulated agreement of the parties, which was incorporated as a part of the Commission's decision in this case, provides for the continuation of a special reduced rate schedule for Pennzoil's customers who are recipients of Social Security Supplemental Security Income (SSI) benefits (HED, Appendix A, p. 8).

8. Senate Bill No. 110, which amended *West Virginia Code* § 24-2A-1, *et seq.* to require for a twenty percent discount for gas and electric service provided to eligible customers during the winter heating months, has been adopted and implemented. This legislative program applies to Pennzoil's customers who are SSI recipients.

CONCLUSIONS OF LAW

1. In this case it is reasonable to continue to establish an appropriate price for Pennzoil's West Virginia utility gas production according to the wellhead prices paid by Pennzoil to nonaffiliated producers from March 12, 1984 through March 11, 1985, the first full year that rates established by this case shall be in effect. Pennzoil shall therefore be required to submit this calculated number to all parties, with supporting documentation, for review and ultimate Commission approval. Since we will provide for Pennzoil's gathering costs at 86¢ per Mcf (See Staff Exh. No. 4 and Staff Exh. No. 5, Sheet 1 of 5) and production taxes at 8.63%, the producer prices utilized to derive this number should exclude any gathering allowance and production taxes.

2. Since the legislative program providing a 20% discount for gas and electric service to eligible customers during the winter heating season addresses the matter of

redistribution of burdens placed on low income customers by increasing utility bills, we determine that it is inappropriate to continue a selective experimental program which redistributes associated burdens in an alternate manner. Therefore, we shall require Pennzoil to remove the special rate schedule for SSI customers from its tariff, effective upon the date of this Order.

ORDER

IT IS, THEREFORE, ORDERED that:

1. The rates and charges set forth in Appendix B, attached to our February 21, 1984 decision in this case, are to be modified to reflect the repricing of Pennzoil's West Virginia gas production according to the projected price paid by Pennzoil to nonaffiliates, exclusive of gathering costs and taxes, during the period of March 12, 1984 through March 11, 1985. The recoverable price of Pennzoil's West Virginia production shall be determined to be this nonaffiliated proxy, plus 86¢ per Mcf gathering costs and production taxes of 8.63%.

2. Pennzoil Company shall calculate the price of Pennzoil's West Virginia production according to the method set forth above and shall submit this calculated number, with supporting documentation, to the Executive Secretary of the Commission and all parties of record in this proceeding within thirty (30) days of the date of this order.

3. Pennzoil Company shall, within thirty (30) days of the date of this order, file a recalculated cost of service and tariffs for Commission approval containing the recoverable cost of Pennzoil's West Virginia gas production as set forth above.

4. Any comments by the parties regarding the accuracy of Pennzoil's calculation or the reasonableness of the projected wellhead prices paid to nonaffiliated pro-

ducers by Pennzoil, as set forth by Pennzoil's supporting data, shall be submitted in writing to the Executive Secretary of the Commission within fifteen (15) days after Pennzoil has filed its calculation and supporting data.

5. As of the date of this order, Pennzoil Company shall no longer provide general service to SSI recipients under the rate schedule established by the parties' stipulated agreement and the Commission's February 21, 1984 decision, as provided by Schedule No. 3 of Appendix B, attached to that decision.

6. The Executive Secretary is hereby directed to serve a copy of this order upon all parties of record by United States First Class Mail.

A Copy.

Teste:

/s/ Lettie Laird
LETTIE LAIRD
Acting Secretary

Commissioner Casto did not participate in this decision.

APPENDIX D

Natural Gas Policy Act of 1978
Section 602, 15 U.S.C. § 3432.

SEC. 602. EFFECT ON STATE LAWS.

(a) AUTHORITY TO PRESCRIBE LOWER MAXIMUM LAWFUL PRICES.—Nothing in this Act shall affect the authority of any State to establish or enforce any maximum lawful price for the first sale of natural gas produced in such State which does not exceed the applicable maximum lawful price, if any, under title I of this Act.

(b) COMMON CARRIERS.—No person shall be subject to regulation as a common carrier under any provision of Federal or State law by reason of any transportation—

(1) pursuant to any order under section 302(c) or section 303(b), (c), (d), or (i) of this Act; or

(2) authorized by the Commission under section 311(a) of this Act.

APPENDIX E

—— U.S. ——, 103 S. Ct. 3564

UNITED STATES SUPREME COURT

No. 81-1672

PENNZOIL COMPANY,

Petitioner,

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA

Former decision, 456 U.S. 959, 102 S. Ct. 2033.

July 6, 1983. On petition for writ of certiorari to the Supreme Court of Appeals of West Virginia. The petition for writ of certiorari is granted. The judgment is vacated and the case is remanded to the Supreme Court of Appeals of West Virginia for further consideration in light of *Public Service Commission of the State of New York v. Mid-Louisiana Gas Company,* 463 U.S. ——, 103 S. Ct. 3024, 76 L.Ed. 2d —— (1983).

APPENDIX F

STATE OF WEST VIRGINIA

At a Regular Term of the Supreme Court of Appeals continued and held at Charleston, Kanawha County, on the 8th day of November, 1984, the following order was made and entered, to-wit:

Case. No. 83-333-G-42T

No. 16513

PENNZOIL COMPANY, a corporation,
Petitioner

vs.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Respondent

THE CONSUMER ADVICATE [sic] DIVISION OF THE PUBLIC SERVICE COMMISSION OF WEST VIRGINIA,
Party Respondent

Upon petition for an appeal from, suspension and review of the final order of the Public Service Commission of West Virginia made and entered on August 10, 1984.

This day came the petitioner and respondent by their respective counsel, pursuant to the Court's order entered in this proceeding on the 13th day of September, 1984, fixing this date for hearing upon the petition filed herein on the 10th day of September, 1984, and the Public Service Commission tendered and filed all papers, documents, evidence, and records, or certified copies thereof, which were before the Commission at the hearing which resulted in the order complained of herein, together with a written statement of its reasons for the entry of said order filed November 2, 1984. And the Court having maturely considered the petition and exhibits, with certificate of service, petition and note of argument of intervenor, The Consumer Advocate of The Public Service Commission, the original record, the statement of reasons of the Commission, and the argument of counsel thereon, is of opinion to and doth hereby grant the appeal, suspension and review of said order of August 10, 1984, of as prayed for in said petition.

It is further ordered that copies of this order shall be delivered forthwith to the Secretary of the Public Service Commission; Goodwin and Goodwin and C. E. Goodwin, John B. Chapman, Baker & Botts, Bruce F. Kiely and Kirk K. Van Tine, counsel for the petitioner, Pennzoil Company, a corporation; Robert R. Rodecker and Daniel L. Frutchey, counsel for the respondent Public Service Commission of West Virginia; Denise C. Goulet, Deputy Consumer Advocate, counsel for the intervenor, The Consumer Advocate Division of the Public Service Commission; as due notice to them of the entry hereof.

A True Copy

Attest: /s/ George W. Singleton
Clerk Supreme Court of Appeals

APPENDIX G

REGULATIONS

§ 270.203 PIPELINE, DISTRIBUTOR, AND AFFILIATE PRODUCTION.

(a) *General rule.* The definition of first sale in section 2(21) of the NGPA includes gas produced by an interstate pipeline, intrastate pipeline, local distribution company, or any affiliate thereof.

(b) *Intracompany transfer.*—(1) *First sales by interstate pipelines.* A transfer, at the wellhead, of gas produced by an interstate pipeline company's production divisional unit to its transmission divisional unit is that pipeline's first sale under the NGPA. It must be evidenced in an intracompany operating statement.

(2) *First sales by intrastate pipelines.* A transfer, at the wellhead, of gas produced by an intrastate pipeline company's production divisional unit to its transmission divisional unit is that pipeline's first sale under the NGPA.

(3) *First sales by a local distribution company.* A transfer, at the wellhead, of gas produced by a local distribution company's production divisional unit to its transmission divisional unit is that company's first sale under the NGPA.

(c) *Circumvention rule for certain sales by affiliates.* Any sale by an affiliate of an interstate pipeline, intrastate pipeline, or local distribution company, that is not itself such a pipeline or local distribution company is that affiliate's first sale under the NGPA unless the Commission, on application, determines not to treat such sale as a first sale.